F. Market Share Must Be Evaluated Whenever Regulatory Relief Is Proposed For Dominant Carriers

The Commission has a long history of considering the regulated provider's market share in determining whether to ease regulatory constraints.[39/] In this instance, however, the Commission expresses a reluctance to rely on market share measurements when assessing competition for the purposes of triggering Phase 2 relief, claiming to identify "drawbacks" in deriving and using this information.[40/] Thus, when determining when to implement Phase 2 deregulation under its market-based approach, the Commission would prefer to exclude market share measurements. In other words, if such a proceeding were conducted today, an ILEC's market share would not be included as one of the factors to consider, even if comparable to the Commission's estimated 99.7 percent market share applicable to all ILECs.

An alleged lack of data is one of the many reasons propounded for the apparent reluctance to include market share measurements when evaluating the "demonstrated presence of competition." Also identified is the difficulty of determining the appropriate market to be measured and the unit of measurement. Whatever merit these concerns may

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39/ Notice at ¶ 203, citing *Price Cap Second FNPRM* at 921; *see also Competition in the Interstate Interexchange Marketplace*, CC Docket No. 90-132, Report and Order, 6 FCC Rcd 5889-90, ¶ 49-51 (1991) (*Interexchange Order*); *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Therefor*, CC Docket No. 79-252, Notice of Inquiry and Proposed Rulemaking, 77 FCC 2d 308 (1979) (*Competitive Carrier Proceeding*).

40/ Under the proposed market-based approach, the Commission need not evaluate the state of competition prior to triggering Phase One relief, because "potential" competition is sufficient to trigger that relief.

have, they offer no basis for excluding a market share analysis. The Commission has undertaken these complex tasks in the past and presumably is competent to undertake them today. Perceived difficulty is not a sufficient basis to deviate from long-standing practice, particularly when the expert agency proposes no alternative. As an invaluable tool in providing context for regulatory action, the Commission should retain a market share analysis anytime it proposes to relax regulation over dominant carriers.

Perceived drawbacks to the use of market share measurements may reflect a recognition that there exists a mismatch between the local exchange competition that would be measured and the regulatory flexibility for exchange access services for which ILECs may qualify under a "market-based" approach. The Commission has identified its third goal of access charge reform as "deregulating incumbent LEC exchange access services as competition develops in the local exchange and exchange access market."[41/] Though this goal refers to a singular market, local exchange and exchange access have been long recognized as two distinct markets having distinct regulatory attributes.[42/] Including market share measurements as a part of the regulatory assessment of competition highlights the mismatch, while excluding those measurements allows the deregulation of ILEC exchange access services without the need to address this mismatch

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41/ Notice at ¶ 14.

42/ If local exchange and exchange access are truly viewed as a single market, then it is both illogical and contravenes economic principles to maintain a distinct access charge regime.

or make any showing that measurable competition in fact has developed in either the local exchange or exchange access markets.

In each of the prior proceedings involving market share analysis, that analysis comprised only one of many factors which the Commission considered, a point the Notice overlooks: "[a]n analysis of the level of competition for incumbent LEC services based *solely* on an incumbent LEC's market share at one time may not provide an adequate basis for us to conclude that a competitive presence truly exists."[43/] The perceived drawback to market share measurements thus results from a misstatement of the role that such measurements play.

Market share measurements are crucial whenever regulatory relief is proposed for dominant carriers. While not the only factor to consider, "market share figures are relevant [ ] to the BOCs' ability to exercise market power."[44/] In determining whether to grant regulatory flexibility, it would be wrong for the Commission to exclude information that measures the incumbent's ability to exercise market power.

43/ Notice at ¶ 203 (emphasis added). The wording of this sentence suggests that regulatory flexibility may be a pre-ordained result once the ILEC files a request to trigger the next phase.

44/ *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-128, FCC 96-388, Report and Order, ¶ 230 (rel. Sept. 20, 1996) (Payphone Order).

III. DISMANTLING THE INTERSTATE ACCESS CHARGE REGIME IS CONSISTENT WITH THE 1996 ACT

Responsive to Section IV: Approaches to Access Reform and Deregulation

Rather than create and endorse a system in which the ostensibly-regulated entity sets rates, the Commission could take a different approach, one which is pro-competitive and deregulatory. Under this alternative, the ILECs' Section 251(c) duties are construed to extend to *all* requesting telecommunications carriers regardless of the specific services to be offered, a position advocated by API and others in response to the *Interconnection NPRM.* The statutory provisions thus would govern the costing and pricing of what are currently considered access services and interconnection agreements would displace the existing access charge regime.[45/]

This alternative recognizes that "[w]hether traffic originates locally or from a distant exchange, transport and termination of traffic by a particular LEC involves the same network functions. Ultimately, the rates that local carriers impose for the transport and termination of local traffic and for the transport and termination of long distance should converge."[46/] By dismantling a regulatory construct that distinguishes between interconnecting carriers and ILEC access customers, the Commission will allow these

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45/ *See* Notice at ¶ 54.

46/ Notice at ¶ 9.

rates to converge and facilitate its stated goal of "end[ing] up with access charge rate structures that a competitive market for access services would produce."47/

A separate rate structure for exchange access services purchased by IXCs may be nothing more that a historical vestige rendered obsolete by both competitive and legal developments. As explained by the Commission, the system was intended "to promote competition in the interstate, interexchange market by ensuring that all IXCs would be able to originate and terminate their traffic over incumbent LEC networks at just, reasonable, and non-discriminatory rates."48/ That purpose has been served: there is no question about the competitiveness of the interexchange market, a market in which AT&T is one of many players rather than the dominant figure. The sole remaining rationale for the interstate access charge regime - to generate revenues sufficient to cover costs and subsidize local services - has been usurped by Section 254, which requires that any subsidy elements be explicitly identified and funded. Since the Commission itself considers the existing regime "fundamentally inconsistent with the competitive market conditions that the 1996 Act attempts to create," it may be more reasonable to dismantle that regime than to attempt to reform it.49/

Though a bold move, it is entirely consistent with and advances the goals of the 1996 Act by removing at least two regulatory structures that appear to have outlived their

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47/ Notice at ¶ 13.

48/ Notice at ¶ 6.

49/ Notice at ¶ 6.

intended purposes and usefulness: the Part 69 rules governing interstate access and the Part 36 rules governing jurisdictional separations.[50] By allowing rates for local and long-distance transport and termination to converge, it avoids the prospect of marketplace distortions resulting from different price signals for "the same network functions." It facilitates competitive entry in what can be expected, otherwise, to remain a monopoly bottleneck. And it ensures that competing carriers have a right to obtain access services at just and reasonable rates, to the benefit of all end-users.

IV. THE PRESCRIPTIVE APPROACH ENSURES THAT ILECS CHARGE JUST AND REASONABLE RATES

Responsive to Section VI: Prescriptive Approach to Access Reform

Unlike a market-based approach, the prescriptive approach offers some degree of assurance that incumbent LECs will comply with their statutory duties to charge just and reasonable rates and not engage in discriminatory or preferential practices. Consequently, it is to be preferred over any approach that relies, in whole or in part, on marketplace forces to reduce rates.

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[50] The Commission has previously "found that interstate and intrastate services are largely provided over common facilities, and that the record contained no evidence that there was an economically meaningful way to divide and measure the facilities used for the provision of interstate service from facilities used for provision of intrastate service." Price Cap Performance Review for Local Exchange Carriers, Fourth Further Notice of Proposed Rulemaking in CC Docket No. 94-1, 10 FCC Rcd 13659, ¶ 63 (1995) (*Price Cap Fourth FNPRM*).

A. Interstate Access Rates Based On Forward-Looking Economic Costs Encourage Competition By Sending Accurate Price Signals

Although the Commission is concerned that the prescriptive approach would require that it play a greater role in the telecommunications marketplace than a market-based approach, that greater role is warranted because exchange access markets are not yet competitive. Commission oversight remains critical until competition is sufficiently established to drive prices towards forward-looking economic costs. Withdrawal from that role must be gradual and predicated only on increasing levels of actual competition in exchange access markets. A TSLRIC or TELRIC approach is critical.

As the industry's response to price cap regulation indicates, ILECs operating in a non-competitive market have little or no incentive to reduce rates. Rules that simulate competitive pressures have failed to drive prices towards economically efficient levels. Consequently, the Commission must prescribe specific rates to accomplish that which the ILECs are unwilling to do on their own.

When establishing rates under a prescriptive approach, the Commission must ensure that it sends accurate price signals with respect to each rate component, excluding as many non-cost considerations as possible. Only economically efficient competitors can exert sufficient downward pressure on ILEC exchange access rates to generate the marketplace forces referred to in the Notice.[51] Prescriptive rates based on forward-looking economic costs must remain in place until efficient competitors are established.

Inaccurate common cost allocations must be avoided. Such allocations will distort the price signals sent by prescribed rates. The Commission therefore should resist ILEC efforts to allow the allocation of "large" or "significant" amounts of common costs to exchange access services, or adopt some intermediate option of determining an "equitable" allocation.[52] Instead, consistent with its long-standing policy of adopting rules that attempt to emulate competitive markets, the Commission should limit permissible allocations to the level that a competitive market would tend to allow. Anything more represents a level of insularity that an entity operating in a competitive market does not enjoy. If the common cost allocation does not reflect an economically efficient level, then neither will the rate.

B. Regulatory Adjustments Can Guarantee Access Rate Reductions With Minimal Further Delay

In addition to emulating a competitive market, a common cost allocation limited to that allowed in a competitive market minimizes administrative burdens, a stated Commission concern. Those burdens can be further minimized by adopted the proposal to reinitialize price cap indices (PCIs) applicable to an incumbent LEC's baskets.

51/ This analysis is consistent with the Commission's observations concerning the terminating access market, in which CLECs are responding to inaccurate price signals.

52/ *See* Notice at ¶¶ 221, 238.

As the Commission recognizes, PCI reinitialization would "simply lower rate levels. It would not guarantee that the incumbent LECs' rate structures would be reasonable."[53] While the concern regarding rate structures may be valid, the long-term objective should not undermine near-term improvements. Reinitialization represents a necessary transitional mechanism to reduce LECs' inflated access rates *without further delay* to the immediate benefit of end users to whom those rate reductions should ultimately flow.

Reinitializing rates on the basis of a TSLRIC or TELRIC study may entail significant time to accomplish, to the detriment of all telecommunications users.[54] Consequently, rates should be reinitialized as soon as possible upon conclusion of this proceeding, based on a revised rate of return as prescribed by the Commission.[55] Administrative burdens associated with represcribing a rate of return cannot be so significant as to warrant further delay in the long-overdue effort to drive access rates closer to economic costs.

Also long-overdue are adjustments to the X-Factor, or productivity offset, which under price cap regulation provides downward pressure on access rates. Both

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53/ Notice at ¶ 223.

54/ That goal is nonetheless commendable, since "the cost showing contemplated by the price cap rules is, in essence, a traditional, embedded-cost rate case." Notice at ¶ 235. Presumably, these TELRIC- or TSLRIC-based rates would constitute the ILECs' new price caps under a prescriptive approach to access reform.

55/ *See* Notice at ¶ 228.

individually and as a member of the CARE Coalition, API has advocated a significant X-Factor increase. Because the X-Factor affects interstate rates only, API has also advocated an interstate-only calculation methodology rather than the "total factor productivity" (TFP) methodology which encompasses data, including input prices and productivity growth, for both the interstate and intrastate jurisdictions. Sharing mechanisms remain a necessary component of the price cap regime until the emergence of actual competition, although sharing obligations may be eliminated for those price cap LECs that select an aggressive X-Factor.

The record in the *Price Cap Fourth FNPRM* offers a compelling basis for substantial increases in the X-Factor. TFP studies filed by members of the CARE Coalition, for example, show that the LECs have been able to achieve interstate productivity of as much as 9.9 percent over the last five years, although the highest current X-Factor option is 5.3 percent.[56/]

The Commission should revise promptly its price cap regulatory regime to institute productivity offsets that bear some reasonable prospect of comporting with marketplace realities. Delay only further deprives telecommunications users of the productivity gains enjoyed by price cap LECs.

[56/] Presentation of CARE Coalition in CC Docket No. 94-1, filed April 16, 1996, *cited in* Notice at fn. 302.

V. RESTRUCTURED RATES SHOULD NOT SHIFT COSTS TO END USERS WITHOUT A SHOWING OF NECESSITY

Responsive to Section III: Rate Structure Modifications

A. The Commission Lacks Any Cost Basis Upon Which To Predicate SLC Increases

The Commission is absolutely correct in concluding that "establishing more economically rational rate structure rules is a necessary first step in the new procompetitive era."[57] Consequently, it is appropriate to eliminate usage-sensitive carrier common line (CCL) charges for the recovery of costs determined, as a general rule, not to be traffic-sensitive.[58] It is not appropriate, however, to replace revenues formerly generated by CCL charges by increasing subscriber line charges (SLCs) , whether by (1) imposing ISDN SLCs on any basis other than "per-facility" or (2) increasing or eliminating the cap applicable to multi-line business and secondary residential lines. The record lacks any basis to conclude that the SLCs currently fail to recover the per-line forward-looking economic loop costs that are properly assignable to the interstate jurisdiction.

The loop costs that the SLC was designed to recover are predicated on the allocation of ILEC embedded loop costs to the federal jurisdiction. Those embedded

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57/ Notice at ¶ 56.

58/ Notice at ¶ 59.

loop costs, which were established in the 1980s, are clearly outdated. Inflated by jurisdictional misallocations, they have remained constant despite the declining-cost nature of telecommunications and despite cost savings that price cap regulation may have spurred.[59] It violates the core principles of economic costing upon which the Commission's restructuring is premised to take any action that increases a customer's SLC until record evidence supports the need to increase that rate.

B. ISDN SLCs Should Be Assessed Only On A Per-Facility Basis

The Commission notes that in its ISDN SLC NPRM, "[a]ll of the commenting parties except AT&T oppose our current rule that assesses a SLC per derived channel. Almost all of the LECs, user groups, equipment manufacturers, IXCs, and other commenters support a rule that would assess a SLC for each pair of copper wires, or a SLC for each ISDN facility."[60] Under a "per-facility" approach, users of derived channel services would pay one SLC for each physical facility through which the services are provided.

The 1996 Act affirms the consensus that only one SLC should be assessed on services, such as ISDN, that enable multiple equivalent channels to be derived from a

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59/ Price cap regulation relies on simulated marketplace pressures to provide price-cap ILECs with incentives to drive costs down by reducing and eventually eliminating technological and managerial inefficiencies. The SLCs have not been reduced to reflect cost savings generated during the six years of price cap regulation.

60/ Notice at ¶ 69.

single telephone line or other communications facility. A per-facility assessment is consistent with and furthers the stated policy of the United States "to preserve the vibrant and competitive free market that presently exists for the Internet and other interactive computer services, unfettered by Federal or State regulation." [61/]

Though the Commission does not specifically request comment on the issue, it appears to be considering an approach that deviates from both the industry consensus and the policies of the 1996 Act. That approach, initially sponsored by U.S. West in the *ISDN SLC* proceeding, would impose SLCs based on the ratio of non-traffic sensitive costs of ISDN service to standard analog service. Based on ILEC cost data, the cost ratios are identified as 1.24:1 for BRI ISDN service and "roughly" 10.5:1 for PRI ISDN service.[62/] The use of ratios to establish BRI and PRI, ISDN SLCs was soundly and correctly denounced in reply comments.[63/]

SLC increases shift costs to end users. Calculating ISDN SLCS on the basis of the aforementioned ratios ensures that users of any telecommunications service that derives multiple channels from a single telephone line or facility will be confronted with substantial rate increases. PRI ISDN users, for example, would pay an amount equal to 10.5 or 11 times their current SLC levels. BRI ISDN users would face significant

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61/ Notice at ¶ 282, *citing* 47 U.S.C. § 230(b)(2).

62/ Notice at ¶ 70. Those costs presumably reflect ILEC embedded costs rather than the forward-looking economic costs that are the goal of this proceeding.

63/ *See, e.g.*, Joint Reply Comments of America Online Inc., CompuServe Inc., and GE Information Services, Inc. (AOL et. al.) at 6.

increases, as well. The record in the *ISDN SLC* proceeding establishes that such rate increases will generate substantial negative effects for both consumer and business users of the Internet and other interactive computer services.[64/] Until it has been established that current rates fail to recover the per-line forward-looking economic loop costs that are properly assignable to the interstate jurisdiction, ISDN SLCs should be assessed on a per-facility basis.

C. SLC Caps Must Be Retained for Multi-Line Business Lines

As an alternate recovery mechanism of non-traffic sensitive costs, the Commission proposes to increase or eliminate the SLC cap for multi-line business and secondary residential lines. This proposal would encompass Internet access providers, which the Commission considers multi-line business customers.[65/] The Commission's proposal is predicated, in part, on Joint Board recommendations that (1) the current $3.50 cap on primary residential and single-line business lines should not be raised; and (2) universal service support should not be provided for multi-line business or residential connections beyond the primary residential connection.[66/]

64/ *See, e.g.*, Joint Comments of AOL et. al. at 6-12; API Comments at 2-3, 5; National Public Radio Comments at 4-5; and United States Telephone Association Comments at 3-4.

65/ Notice at ¶ 285.

66/ Notice at ¶ 64.

Increasing or eliminating the SLC cap is warranted only if the Commission concludes that the current rate fail to recover current, economic per-line loop costs that are properly assigned to the interstate jurisdiction. The record appears to lack any basis upon which to make such a determination, as well as a determination as to the amount of any alleged shortfall. Indeed, compelling arguments can be made that SLC reductions are more appropriate, given the use of outdated, embedded costs in a declining-cost industry, cost savings generated during the six years of price cap regulation, and the Commission's recognition of the jurisdictional cost misallocations mandated by current separations rules.

Moreover, increasing the SLC for some customers, while retaining capped rates for others, raises serious issues regarding compliance with Section 254 since it suggests an implicit subsidy between classes. While the 1996 Act does not prohibit subsidies, they must be "specific, predictable and sufficient."[67/] The Commission may be incapable of complying with this statutory mandate if it lacks an adequate basis upon which to explicitly identify the subsidy (if any) that a capped SLC would necessitate.

67/ 47 U.S.C. § 254(b)(5).

VI. SAFEGUARDS AND PUBLIC INTEREST FINDINGS MUST ACCOMPANY DEREGULATION OF SUBSTANTIALLY COMPETITIVE SERVICES

Responsive to Section IV(B): Approaches to Access Reform and Deregulation: The Goal: Deregulation in the Presence of Substantial Competition

A. Safeguards and Public Interest Findings Are Consistent With Commission Policy And The 1996 Act

Deregulation of services subject to substantial competition is a laudable goal. In a substantially competitive environment, the incumbent LEC no longer possess sufficient market power to control market prices for a given service.[68/] However, before the Commission deregulates any ILEC access service, it must ensure that deregulation is consistent with the public interest and accompanied by appropriate safeguards. Neither requirement is inconsistent with the spirit or letter of the 1996 Act.[69/]

The regulatory freedom that certain ILECs may enjoy as a result of "substantial competition" far exceeds that extended to AT&T when it was found to face "substantial competition," or the relief proposed for price cap LECs as recently as September, 1995.[70/] Under the Commission's proposal, ILEC access services subject to substantial

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68/ *Interexchange Order* at ¶ 60.

69/ *See e.g.,* Section 10(a), relating to regulatory forbearance; Section 271(c)(3), relating to BOC entry into in-region interLATA markets; Section 272, relating to BOC separate affiliate safeguards; Section 273(d)(3), relating to BOC manufacturing safeguards; Section 274(a), (b), relating to BOC electronic publishing safeguards; Section 275(a), (b), relating to delayed entry and nondiscrimination requirements applicable to BOC alarm monitoring services; and Section 276(a), (b), pertaining to nondiscrimination safeguards for BOC payphone services.

70/ *See Interexchange Order* at ¶ 188; *Price Cap Second FNPRM* at ¶ 3.

competition would be exempted from tariff and price cap regulation. The ILEC would then operate outside Commission purview with respect to these services.[71] AT&T services subject to substantial competition, on the other hand, continued to receive Commission scrutiny, although further tariff streamlining and contract carriage reduced the level of that scrutiny. Similarly, under the Commission's 1995 proposal, price cap LECs able to demonstrate substantial competition for particular services within a geographic market would qualify for streamlined regulation and removal of those services from price cap regulation in that market.

If the Commission elects to deregulate, then it must be certain that the regulatory freedom will not be abused. At a minimum, a "public interest" test and the imposition of competitive safeguards are necessary to fulfill this function.

The public interest test and accompanying safeguards are all the more critical because the Commission has conceded that the exchange access market currently constitutes a "monopoly bottleneck stronghold."[72] Indeed, in the instant Notice, the Commission expresses its concern that "even with a competitive presence in the market, terminating access may remain a bottleneck."[73]

Deregulation is not warranted for those ILECs that continue to exercise market power with respect to specific services, although some lesser form of regulatory relief

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71/ Notice at ¶ 149.

72/ *Interconnection Order* at ¶ 4.

73/ Notice at ¶ 271.

may be appropriate, depending upon the level of competition each faces. Regulatory relief on a carrier-specific basis is consistent with the *Interexchange Order,* in which the Commission limited its focus to a single carrier: AT&T.

B. It May Be Appropriate To Remove From Price Cap Regulation High Capacity Special Access Services Offered by Some Carriers in Some Areas

In apparent furtherance of its stated goal to deregulate in the presence of substantial competition, the Commission asks whether special access services offered by price cap LECs at speeds of DS1 or higher should be removed immediately from price cap regulation.[74] These services presumably would remain subject to tariffing requirements, thereby providing the Commission with some continuing oversight role. While the record is unlikely to support a blanket finding applicable to all price cap LECs in all geographic markets, a more narrowly-tailored deregulatory initiative may be warranted. In particular, removing these services from price-cap regulation may be appropriate for certain specified carriers if (1) the record demonstrates that these specific ILECs, despite their marketplace advantages, are unable to preclude the effective functioning of a competitive market in high-capacity special access services and (2) accompanied by certain safeguards and public interest findings.[75]

74/ Notice at ¶ 153.

75/ *See Interexchange Order* at ¶ 60.

As the basis for its query, the Commission notes that many incumbent LECs contend that for certain geographic markets these special access services "are already subject to intense competitive pressures that today discipline incumbent LEC pricing of such services."[76] The Notice, however, lacks any information or conclusions regarding the degree of competition that exists, including quantification.

Responsive comments may include information and data, including market share measurements, adequate for the Commission to conclude that certain ILECs no longer possess sufficient market power to control market prices for high-capacity special access services in densely-populated urban areas. If so, then only the high-capacity special access services offered by these specific ILECs should be removed from price cap regulation and, then, only in those geographic areas in which the ILECs no longer exercise market power. As suggested by the Commission, these geographic areas could conform to the areas implemented by the relevant state in making unbundled network elements available to competitors.[77] It would appear reasonable to include areas served by competing facilities-based carriers, in the event those networks extend beyond the implementation area identified by the relevant state.

In addition to conducting a public interest determination, the Commission must also implement safeguards to ensure that these ILECs do not compensate for the lower

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76/ Notice at ¶153.

77/ Notice at ¶155.

revenues derived from the deregulated market(s) by increasing rates for these services in less competitive areas. Other safeguards may be appropriate, as well.

VII. TRANSITION MECHANISMS MUST NOT SERVE AS REVENUE GUARANTORS FOR ILECS FACING COMPETITIVE PRESSURES

Responsive to Section VII: Transition Issues

Though it ushered in sweeping changes in ILEC pricing, the 1996 Act does not mandate that the Commission provide for, or that incumbent LECs receive, revenues to offset the difference between access charges based on interstate-allocated embedded costs and the forward-looking economic costs of providing access services (hereinafter, "the gap").[78/]

According to AT&T estimates, this gap may be as large as $11 billion as of November, 1996.[79/] Universal services subsidies, recovery of under-depreciated amounts, and revenues derived from new competitive opportunities will be among the factors contributing to narrow that gap. The parties are certain to further narrow that gap by identifying significant sums relating to factors such as over-built plant, excessive expense associated with customer and corporate operations, inefficiencies, and earnings in excess

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78/ Though they may be applicable to ILECs subject to traditional rate-based regulation, API's comments on this issue are directed to price-cap ILECs.

79/ Notice at ¶ 11.

of authorized rates of return.[80] Nonetheless, the Commission faces a significant challenge in determining the most appropriate approach to resolving the issues associated with this gap.

A. ILECs Are Not Entitled To Transitional Assistance

As a starting point, the Commission should recognize that the ILECs are not *entitled* to transitional assistance. Though the industry regularly cites the "regulatory compact" as justification for its claims, that compact - if it ever existed - was broken long ago, as the introduction of price cap regulation in 1991 confirmed. With the 1996 Act, Congress eliminated any vestige of that compact. Competitive entry is a cornerstone of that Act, which demands "fundamental changes in the structure and dynamics of the telecommunications industry."[81] In this fundamentally altered industry, the Commission must reject entitlement claims premised on law or arguments grounded in rate-of-return or rate-based regulation, particularly when asserted by carriers subject to price cap or alternative regulation.[82]

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[80] *See* Notice at ¶ 247.

[81] Notice at ¶ 5.

[82] Congress specifically rejected reference to a rate-of-return or other rate-based proceeding as a basis for setting nondiscriminatory, cost-based rates (which may include a reasonable profit) for interconnection and unbundled network elements. Section 252(d)(1).

If equity considerations drive a Commission decision to allow recovery, those considerations must not be one-sided. The Commission must consider the impact upon both competitors and end-users. Until access charge reforms are fully implemented, and all transition mechanisms eliminated, both carriers and customers will shoulder the burdens associated with inflated rates. The more gradual the reform, the longer these burdens must be borne, in apparent violation of statutory standards that require just and reasonable charges, practices, classifications, and regulations.[83/]

B. Transitional Assistance Must Be Confined To Revenue Losses Directly Attributable To Regulatory Action

Equity considerations, moreover, require that any transition mechanism be very narrowly circumscribed to compensate ILECs only for those negative revenue impacts that can be directly attributed to federal regulatory actions, such as the under-depreciation of ILEC assets.[84/] The ILECs should not be compensated for their inability, on a going-forward basis, to charge amounts that exceed "just and reasonable" rates because compensation for these sums is akin to retaining the excessive rates. Nor should a

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83/ Though no time periods are provided, the Commission anticipates a "gradual" reform under a market-based approach. Notice at ¶ 261.

84/ Notice at ¶¶ 249-50. The equity of reimbursing incumbent carriers may be affected to the extent that the ILEC industry advocated, and presumably benefitted from, a particular action.

transitional mechanism compensate for amounts attributable to inefficiencies or over-investment.

Price-cap ILECs have had six years in which to respond to primarily competitive, as opposed to regulatory, incentives. As the Commission explains, ILEC price cap regulation "is designed to simulate some of the efficiency incentives found in competitive markets and to act as a transitional regulatory scheme until the advent of actual competition makes price cap regulation unnecessary."[85/] By replicating competitive incentives, price cap regulation encourages price cap LECs to make economic decisions similar to those they would make in a fully competitive market.[86/] Pleas for transitional mechanisms encompassing embedded costs demonstrate that the ILECs have not responded to those simulated competitive incentives. Had they in fact made such decisions in a fully competitive market, they would not now be asserting that access services priced at forward-looking economic cost - even after considering the receipt of anticipated universal service subsidies - will impose revenue losses.[87/] The ILECs should not be rewarded for their refusal to respond to the Commission's efforts to prepare them for a competitive market.

85/ Notice at ¶ 30.

86/ Price Cap Performance Review for Local Exchange Carriers, First Report and Order, CC Docket No. 94-1, 10 FCC Rcd 8962, ¶¶ 65, 90-91 (1995).

87/ As demonstrated by the Commission's reference to "egregiously high" terminating access charges, some significant share of the revenue gap must be attributed to monopolistic pricing practices. Notice at n.368.

The marketplace does not provide for transitional devices that cushion the impact of competitive entry and revenue loss. To the extent this type of regulatory construct compensates ILECs for sums unrelated to either the provision of universal services or for the consequences of direct regulatory action, that mechanism contravenes market forces. As such, it also contravenes the Commission's long-standing practice of emulating competitive market forces.

The history of transitional mechanisms, including price cap regulation and the transport interconnection charge, indicates that they assume a permanence unless clearly limited. The Commission must therefore include a sunset provision in any transition mechanism it adopts to compensate ILECs for revenue losses directly attributable to federal regulatory actions. In other words, extension - not cancellation - requires affirmative action. If the Commission fails to explicitly define the duration of any its transition mechanism, it virtually ensures that carriers and customers will continue to pay inflated rates for ILEC access services.

VIII. THE COMMISSION NEED REGULATE ONLY ILEC TERMINATING ACCESS RATES, NOT CLEC RATES

Responsive To Section VIII(A)(2): Other Issues: Regulation of Terminating Access - Non-Incumbent LECs

The Commission's concern over "egregiously high terminating access charge[s]" is well-founded.[88] Its proposal to regulate the rates of both incumbent and competitive LECs is not. Imposing rate regulation on CLECs constitutes peremptory action that conflicts with the principles of dominant carrier regulation that has guided and informed the Commission's decisions over many years.[89]

The Commission acknowledges that it is "extremely reluctant to impose price regulation on non-dominant carrier services without a strong showing that such regulation is necessary."[90] The only showing that demonstrates that such regulation is necessary is a proceeding to determine market dominance, preferably conducted so as to target specific carriers, markets, and services. Absent some record evidence upon which to determine a CLEC's ability to control market prices, there exists little or no rationale for the Commission to impose rate regulation, particularly since such action would appear to contravene the pro-competitive, deregulatory policies of the 1996 Act.

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[88] Notice at n.368.

[89] Notice at ¶ 277.

[90] Notice at ¶ 278.